



June 16, 2010

Financial Services Reg Reform Update: Conference Week 1

It's week 1 of the financial services regulatory reform conference and already, this process looks a lot less open than Chairman Barney Frank had promised. While Members are mugging for the CSPAN cameras, back-room deals are being cut on the tougher provisions after the cameras are shut off. Republicans are left asking, "**Where is the transparency the Democrats promised?**"

Below is a list of the notable sections that will be coming up for debate soon, as well as the scorecard so far...

Republicans Will Fight for Small Business Protection: The House provision that exempts small issuers (less than \$75 million in market capitalization) from the requirements of Sarbanes-Oxley Section 404(b) was included in the House offer.

- Note that this is the Garrett-Adler provision that passed in Committee over Chairman Frank's strenuous objections.

Rewarding the SEC? Look for Republicans to express objections to SEC self-funding mechanism during debate on the SEC. Why should we continue to reward regulators that failed so miserably to predict the crisis?

Bureaucrats Dictate Pay? Chairman Frank supports a provision on Enhanced Compensation Oversight for Financial Industry. House requires all Federal financial regulators to issue and enforce joint compensation rules specifically applicable to all regulated financial institutions. Many Republicans will object to bureaucrats setting pay packages for financial institutions.

Audit the Fed! Rep. Garrett will be offering Dr. Ron Paul's "Audit the Fed" Amendment. Dr. Paul's Federal Reserve Transparency Act currently has 319 cosponsors in the House. With each taxpayer dollar lent during the crisis, Fed officials assured the American people they would not take losses. American taxpayers deserve more than the central bank's assurances; they deserve proof. A full audit of the Federal Reserve System is the only way to create the necessary level of transparency to protect taxpayers.

STILL MISSING FROM THE DEBATE: Reform of Fannie Mae and Freddie Mac, the toxic twins that continue to bleed the taxpayer dry. Apparently, Democrats are simply not concerned about the hemorrhaging of taxpayer dollars into the GSE black hole.



Scorecard So Far

Title IV, Private Funds (hedge funds, etc): Title passed by voice vote in the House; Chairman Frank has rejected Senate counter offer regarding commodity advisors.

Title III, OTS-OCC: Title passed 12-7 in the House; Republicans objected to the retroactive bailout for IndyMac investors but the Democrats can't seem to quite their love affair with spending.

Title V, Office of Insurance: Title passed by voice vote in the House; Chairman Frank disagrees with Senate counter offer; Frank and Dodd are convening a "working group" to resolve issues (will this be televised on CSPAN? We are skeptical)

Title IX, Sec. C: Credit Rating Agencies: Title passed by voice vote; Garrett amendment striking federal implicit support of rating agency ratings in all federal statutes was accepted by voice vote. Frank expresses preference for House's tougher liability standards rather than the text of the Senate counter offer, and staff is working to find a compromise.

FINAL SCORE TO DATE:
Winner – Government Bureaucrats
Loser – American Taxpayers

Fannie & Freddie: The Mother of All Bailouts

By Investor's Business Daily

June 15, 2010



Subprime Scandal: The taxpayer cost of bailing out Fannie Mae and Freddie Mac could be as high as \$1 trillion. Yet Democrats still refuse to reform the toxic twins, making reform meaningless.

Already their \$160 billion government rescue has surpassed the amount spent on AIG, Citigroup and other poster boys of the financial crisis, making their liability "the mother of all bailouts," as one analyst put it.

The failed Washington-based mortgage giants were more exposed to subprime and other junk home loans than any of Washington's favorite Wall Street whipping boys. And they commanded a much larger share of the mortgage market. Together they owned or guaranteed more than half the mortgages and mortgage-backed securities when they collapsed in 2008.

Thanks to their politically mandated lending goals, congressionally chartered Fannie and Freddie were at the heart of the subprime scandal. We can't think of two companies more deserving of overhaul. Only, Congress doesn't even attempt to rein them in. Fannie and Freddie are conspicuously absent from the financial reform bills House and Senate Democrats are cobbling together.

Their private piggy bank for "social justice" - which they used to give high-risk loans to constituents who couldn't otherwise qualify for them or afford them - is safe from Obama's promised "sweeping" overhaul. Overhauling the banking system without fixing Fannie and Freddie is like fighting terrorists without attacking the jihadi ideology motivating them.

This regime intends to broaden the "affordable housing" mission that led to the recent wave of defaults, by creating a Consumer Financial Protection Agency that will see to it that banks and independent mortgage companies alike meet new fair-lending standards. That means even more sloppy underwriting to get the government off their backs.

It's instructive to go back to when this subprime scandal really began. Starting in 2000, HUD required Fannie and Freddie to position fully half their mortgage portfolios in high-risk, low-income loans - despite a spike in subprime foreclosures at the time. The "affirmative action" credit quotas, raised higher still by Bush's two Hispanic HUD secretaries, drove Fannie and Freddie into the subprime market - and eventually into financial insolvency.

The quotas "forced us to go into that (riskier subprime) market to serve the targeted (uncreditworthy) populations that HUD wanted us to serve," said Freddie Mac spokeswoman Sharon McHale.

The administration, with help from the media, is trying to blur that picture by saying that factors other than housing policy played a more fundamental role in creating the crisis. Team Obama fingers the "excesses" of the private sector - namely, lightly regulated derivatives and other complex instruments.

The New York Times recently editorialized that they were "at the heart of the crisis." In fact, they were secondary to the role Fannie and Freddie played. Wall Street simply sliced and diced the bad debt Fannie and Freddie guaranteed - at the behest of HUD and other federal regulators.

The Times went on to argue for passage of the Consumer Financial Protection Agency to expand politically mandated lending to the car industry under a strengthened Community Reinvestment Act. This echoes lobbying by CRA boosters like the Center for Responsible Lending.

"The foreclosure crisis - and the resulting economic crisis - was caused by reckless and predatory lending practices and toxic financial products, not by the Community Reinvestment Act, Fannie Mae and Freddie Mac, or any other policy goal aimed at increasing homeownership," a center spokesman recently testified in arguing for a beefed-up CRA.

Here we go again.

"Flexible underwriting" was codified as part of a 1995 CRA overhaul. Banks that didn't bend their rules to qualify poor and minority loan applicants with bad credit didn't pass the stricter CRA lending test enforced by bank examiners. Fannie and Freddie became models of underwriting "flexibility." True reform should start here.